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TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1932

No. 180

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

R. P. CLARK

ON WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE DISTRICT OF COLUMBIA

PETITION FOR CERTIORARI FILED JUNE 27, 1933
CERTIORARI GRANTED OCTOBER 16, 1933

(36877)

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Before United States Board of Tax Appeals.

[Title omitted.]

Petition

Filed Feb. 9, 1928

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (IT:FAR:B-2:LTC-60D) dated December 21, 1927, and as a basis of his proceeding alleges as follows:

1. The petitioner is an individual with residence at Miami, Florida.

2. The notice of deficiency, a copy of which is attached and marked "Exhibit A," is a true copy of the notice mailed to the petitioner on December 21, 1927.

3. The taxes in controversy are income taxes for the calendar years 1923 and 1925 in the following amounts:

1923	$2,722.41
1925	473.24
Total	3,195.65

4. The determination of tax set forth in the said notice of deficiency is based upon the following errors:

(a) The commissioner erred in computing the petitioner's taxable net income for 1923 in that he failed to allow as a deduction, as provided for in section 204 (d) of the revenue act of 1921, a net loss sustained by petitioner for the calendar year 1921 amounting to $17,768.51 in excess of any taxable income for 1922.

(b) The commissioner erred in computing the taxable net income of petitioner for 1923 in that he failed to deduct from the net income the net loss sustained by petitioner for the calendar year 1922, which net loss amounted to $4,985.18 or more.

(c) The commissioner erred in computing the taxable net income of petitioner for the year 1925 in that he failed to allow as a deduction a loss of $950 sustained by petitioner on the sale of an automobile.

5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

(a) The income-tax return for 1921 filed by petitioner showed a loss of $16,041.21, which loss, upon reaudit by the commissioner was increased to $17,768.51 due to the fact that petitioner had overstated his share of income from the partnership of D. M. Picton & Co.

(b) The loss reported by petitioner was due to the fact that during the year 1921 he was required to pay $68,000 on negotiable
4 paper which he had endorsed at various times for the Bowers Southern Dredging Company, which concern went into the hands of a creditors' committee in June, 1920, and also from a sale of some stock of the same concern at a loss of $9,500.

(c) Petitioner was engaged in the business of dredging and river and harbor improvement work as a partner in the firms of Megathlin & Clark, Miami, Florida; Florida Dredging Company, Miami, Florida; D. M. Picton & Co., Port Arthur, Texas; and as president and majority stockholder of the Bowers Southern Dredging Company, doing the same character of work. Such business has been regularly carried on by petitioner for years and the losses sustained were directly connected therewith.

(d) During the year 1922 petitioner suffered losses from the operations of Megathlin & Clark, Florida Dredging Company, and D. M. Picton and Company, and a loss of $92,500 from the sale of some of his stock in the Bowers Southern Dredging Company in an effort to rehabilitate the business. These losses resulted in a net loss to petitioner in 1922 of $4,985.18, which amount he deducted in determining his taxable income for 1923.

(e) The losses for 1921 and 1922 are deductible in determining the tax liability for 1923 in accordance with section 204 (a) and (b) of the revenue act of 1921.

(f) Petitioner in 1925 purchased an automobile for $5,368.70, paying in cash $3,468.70 and turned in at a value of $1,900 a Cadillac car which had been purchased by him for $5,000. After deducting depreciation on the Cadillac car from date of purchase petitioner sustained a loss of $950.

Wherefore the petitioner prays that this board may hear the proceeding and grant relief by disallowing the deficiencies asserted by the commissioner.

WM. S. HAMMERS,
Attorney for Petitioner, 501 Union Trust Building, Washington, D. C.

[*Duly sworn to by R. P. Clark; jurat omitted in printing.*]

5 *Exhibit A to petition*

IT:FAR:B-2:LCT-60D.

TREASURY DEPARTMENT, WASHINGTON,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Dec. 21, 1927.

Mr. R. P. CLARK,
Post-Office Box 918, Miami, Florida.

SIR: The determination of your tax liability for the years 1923, 1924, and 1925 discloses a deficiency of $3,195.65 for 1923 and 1925, as shown by the attached statement.

In accordance with the provisions of section 274 of the revenue act of 1926, you are allowed 60 days from the date of mailing of this letter within which to file a petition for the redetermination of this deficiency. Any such petition must be addressed to the United States Board of Tax Appeals, Earle Building, Washington, D. C., and must be mailed in time to reach the board within the 60-day period, not counting Sunday as the sixtieth day.

Where a taxpayer has been given an opportunity to file a petition with the United States Board of Tax Appeals and has not done so within the 60 days prescribed and an assessment has been made, or where a taxpayer has filed a petition and an assessment in
6 accordance with the final decision on such petition has been made, the unpaid amount of the assessment must be paid upon notice and demand from the collector of internal revenue. No claim for abatement can be entertained.

If you acquiesce in this determination and do not desire to file a petition with the United States Board of Tax Appeals, you are requested to execute a waiver of your right to file a petition with the United States Board of Tax Appeals on the inclosed Form A, and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:FAR:B-2:LCT-60D. In the event that you acquiesce in a part of the determination, the waiver should be executed with respect to the items to which you agree.

Respectfully,

D. H. BLAIR,
Commissioner.
By C. B. ALLEN,
Deputy Commissioner.

Inclosures: Statement, Form A, Form 882.

STATEMENT

IT:FAR:B-2:LCT-60D.

DEC. 21, 1927.

In re Mr. R. P. Clark, post-office box 918, Miami, Florida.

Year	Deficiency in tax.
1923	$2,722.41
1924	None.
1925	473.24
Total	$3,195.65

The report of the internal-revenue agent in charge at Jacksonville, Florida, transmitted to this office under date of November 29, 1927, has been reviewed and approved.

Your protest was considered at a conference in the office of the internal-revenue agent in charge and it has been recommended that the deduction of $1,575.00 in 1924 for automobile expenses be allowed. Your return has accordingly been accepted as filed.

It has also been recommended that the value of the mortgage obtained in 1925 from the sale of real estate be deemed
7 to have a fair market value of $10,300.00, which amount is the original investment. This recommendation has also been approved by this office.

Your contention that the loss in 1921 is deductible on your 1923 return is not allowable. This loss was incurred in connection with the handling of stock of the Clark Dredging Company and does not constitute a business loss as defined in section 204 of the revenue act

of 1921. Your contentions that a loss of $17,768.51 was not claimed on your 1923 return was also considered. This loss was also incurred in connection with transactions in stock of the Clark Dredging Company. Such loss was not incurred in connection with your trade or business and is not an allowable deduction. The loss of $1,850.00 claimed in 1925 from the sale of an automobile is not allowable. The evidence presented is not conclusive, and the value of the new car which was received in exchange is not stated nor is it stated whether any cash consideration was given. If no cash consideration was given to purchase the new car, no loss is allowable, as the automobile would have been exchanged solely for property of like kind in accordance with section 203 (b) of the revenue act of 1926.

Computation of tax

1923

Net income originally reported		$25,727.82
Interest on tax-free covenant bonds reported	None.	
As adjusted	$12,096.00	
		12,096.00
Income from partnership reported	17,696.23	
As adjusted	17,965.16	
		268.93
Loss as claimed	$4,985.18	
As adjusted	None.	
		4,985.18
Total		$43,077.93
Decrease in dividends		40.00
Total increase as adjusted		43,037.93
8 Amount subject to ordinary taxes		$43,037.93
Dividends and exemption		11,798.07
Amount subject to normal tax		$31,239.86
Total tax at ordinary rates		$5,856.40
Tax on capital net gain of $6,174.00		771.75
		$6,628.15
25% reduction, revenue act of 1924	$1,657.04	
Tax withheld at source	241.92	
		1,898.96
Net tax assessable		$4,729.19
Tax assessed	$2,675.71	
25% reduction, revenue act of 1924	668.93	
		2,006.78
Deficiency		$2,722.41

1925

Net income reported		$45,755.90
Tax-free covenant-bond interest reported	$6,347.66	
Adjusted	9,680.66	
	3,333.00	
Loss on sale of car disallowed	1,850.00	
Increase	5,183.00	

Profit on sale of real estate reported	$6,730.33		
As adjusted	3,350.33		
		$3,380.00	
			$1,803.00
Total income subject to ordinary rates			$47,558.90
Capital net gain reported		None.	
As adjusted		$1,680.00	
			1,680.00
Total income			$49,238.90
9 Income subject to surtax			$47,558.90
Dividends and exemption			30,093.38
Income subject to normal tax			$17,465.52
Total tax			$3,320.35
12½% on capital gain			210.00
Total tax			$3,530.35
Tax on earned income		$51.25	
Tax paid at source		193.61	
			244.86
Net tax assessable			$3,285.49
Tax assessed			2,812.25
Deficiency			$473.24

Payment should not be made until a bill is received from the collector of internal revenue for your district and remittance should then be made to him.

Now, March 18, 1931, the foregoing petition certified from the record as a true copy.

[Seal, U. S. Board of Tax Appeals.]

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

Before United States Board of Tax Appeals

[Title omitted.]

Answer

Filed April 6, 1928

The Commissioner of Internal Revenue, by his attorney,
10 C. M. Charest, General Counsel, Bureau of Internal Revenue, for answer to the petition filed in the above-entitled appeal, admits and denies as follows:

1. Admits the allegations contained in paragraph 1.
2. Admits the allegations contained in paragraph 2.
3. Admits the allegations contained in paragraps 3.
4. Denies that the commissioner committed the errors alleged in paragraph 4.
5. Denies the allegations set forth in paragraph 5.

Denies generally and specifically each and every allegation contained in the taxpayer's petition not hereinbefore admitted, qualified, or denied.

Wherefore it is prayed that the taxpayer's appeal be denied.

(Signed) C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

Of counsel:

J. L. DEVENEY,
Special Attorney, Bureau of Internal Revenue.

JLD.

Now, March 18, 1931, the foregoing answer certified from the record as a true copy.

[Seal, U. S. Board of Tax Appeals.]

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

A true copy. Teste:

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

Before United States Board of Tax Appeals

Docket No. 34824. 19 B. T. A. —

R. P. CLARK, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Findings of fact and opinion

Promulgated May 5, 1930

1. In 1921 the petitioner, who was the majority stockholder and president of a corporation, sustained a loss as a result of having to pay certain notes of the corporation which he had endorsed. In 1921 and 1922 he sustained losses on the sale of stock of the corporation. Held that such losses do not constitute net losses within the meaning of section 204 (a) of the revenue act of 1921.

11

2. Loss on the exchange of an automobile determined.

William S. Hammers, Esq., for the petitioner.

Arthur Carnduff, Esq., for the respondent.

This proceeding is for the redetermination of deficiencies in income tax of $2,722.41 and $473.24 for 1923 and 1925, respectively. The matters in controversy are the action of the respondent (1) in failing to allow as a deduction in computing net income for 1923 the amount of $17,768.51, representing a net loss sustained in 1921 in excess of taxable income for 1922; (2) in failing to allow as a deduction from 1923 net income a net loss of $4,985.18 sustained by the petitioner in 1922; (3) in refusing to allow as a deduction for 1925

as a loss the amount of $950 sustained by the petitioner on the exchange of an old automobile for a new one. An admission made by counsel for the respondent at the hearing has eliminated the issue raised by No. (3).

Findings of fact

The petitioner is an individual residing at Miami, Florida. Since 1888 he has been engaged in the business of dredging and supervising dredging operations off the coast of Florida and elsewhere. He was associated with the Bowers Southern Dredging Company, hereinafter referred to as the Bowers Company, from the time of its organization in 1899 until about September, 1922, when the Clark Dredging Company, hereinafter referred to as the Clark Company, was organized, and took over the business of the Bowers Company. Clark became president of the Bowers Company in 1905 and continued in that capacity as long as it continued to operate. In that capacity he was the active directing head of the corporation and devoted all of his time to its operation. During 1921 and in 1922 until the business was taken over by the Clark Company the petitioner, who was the majority stockholder in the Bowers Company, was the managing operator of the corporation for a committee
12 of its creditors. He was president of the Clark Company after its formation. The Bowers Company was engaged in dredging and other river, harbor, and jetty work.

In addition to his association with the Bowers Company the petitioner in 1921 and 1922 was a member of the partnerships of D. M. Picton and Company, Port Arthur, Texas, the Florida Dredging Company, Miami, Florida, and Megathlin and Clark, Miami, Florida. Megathlin and Clark and the Florida Dredging Company were engaged in the dredging business and D. M. Picton and Company was engaged in river and harbor work and jetty building. The petitioner took an active advisory interest in these partnerships, whose work was mostly in connection with the work of the Bowers Company. In 1921 and 1922 the petitioner also owned stock in a number of corporations which he held as investments.

The authorized capital stock of the Bowers Company when organized in 1899 was $600,000, divided into shares of a par value of $100 each. At the time of organization the petitioner received about 1,800 shares of the company's stock for assets delivered to it. In 1910 the company's capital stock was increased to $750,000 par value. The entire amount of the additional stock was subscribed to by the stockholders and paid for in cash at par by them. By 1922 the petitioner's stockholdings in the company had increased to more than 3,000 shares. The additional shares of stock were acquired by petitioner at $100 per share from time to time, some having been acquired as late as 1914. Prior to 1920 the company paid dividends regularly, and from 1907 to 1917 its stock had a value in excess of par. In 1917 when the war began the stock ceased to have a value equivalent to par.

At the beginning of the war in 1917 the Bowers Company had many contracts to complete and began to have financial difficulties. This finally resulted in its business being placed in the hands of a creditors' committee, under which it was operated in 1921. The company was unable to borrow money from banks without the individual endorsement of petitioner.

In a desire to protect his investment in the stock of the company the petitioner at various times thereafter endorsed notes of the company.

13 In 1921 as a result of his endorsement of the notes of the Bowers Company the petitioner had to pay $68,000 on them. This amount he took as a deduction for losses in his 1921 income-tax return and it was allowed in the final audit of the return by the respondent.

In his return for 1921 the petitioner reported a loss of $7,000 from the sale of stocks, which was explained on the return as follows:

	Cost	Mar. 1, 1913, value	Amount received	Loss
Stock (Bowers Sou. Dredging Company)		$10,000	$500	
" (Galveston Indemnity Co.)	$3,500		1,500	
" (Galveston Hotel Company)	1,000		500	
" (Belcher Asphalt Paving Co.)			5,000	
	$4,500	$10,000	$7,500	$7,000

The loss reported by the petitioner was allowed by the respondent in the final audit of the return. The Bowers Company stock, on which a loss of $9,500 was shown, represented 100 shares of the stock that the petitioner had purchased at $100 a share and which was sold in 1921 for $5 a share, or for $500.

For 1921 the petitioner reported the following items of income:

Salaries, wages, commissions, etc.:	
D. M. Picton and Company	$4,333.34
Creditors' committee, Bowers Company	9,000.00
Income from partnerships:	
D. M. Picton and Company	39,646.51
Megathlin and Clark	707.14
Florida Dredging Company	7,367.94
Dividends on stock of domestic corporations	91.00

In addition to reporting the losses refered to above the petitioner took a deduction of $1,480 as interest paid. In the final audit of the return the respondent found that the petitioner had overstated his income from the partnership of D. M. Picton and Company by $1,727.30. This results in a net loss for 1921 of $17,768.51 instead of $16,041.21 reported by the petitioner.

The petitioner in 1922, being desirous of having some one
14 who was strong financially associated with the business of the Bowers Company, sold 1,000 shares of the stock he owned in that company to George H. Nolan for $7,500. In his return for

1922 the petitioner according took as a deduction for a loss sustained on the sale of the stock the amount of $92,500, which represented the difference between its cost of $100,000 and the selling price. In the final audit of the return the loss was allowed by the respondent.

About September 1, 1922, the Clark Company was organized by the petitioner and took over the assets and liabilities of the Bowers Company. The stock of the Clark Company was distributed to the stockholders of the Bowers Company on the basis of one share in the Clark Company for each two held in the Bowers Company. The Clark Company issued bonds to cover all the liabilities of the Bowers Company. These bonds have since been paid and retired. In 1922 the petitioner received bonds for the amount of money paid by him personally for the benefit of the Bowers Company and in his return for that year reported as income from this source the amount of $58,000.

Upon the organization of the Clark Company the stock acquired by Nolan in the Bowers Company was exchanged for stock in the Clark Company, Nolan becoming vice-president and a director in the latter-named company. By July 15, 1923, the net earnings of the Clark Company amounted to $20 per share. As Nolan had decided to withdraw from the company, the petitioner purchased his stock at what it had cost him (Nolan) plus the earnings thereon of $20 per share.

In his 1922 return the petitioner reported income as follows:

Salaries, wages, commissions, etc.:	
Creditors committee, Bowers Company	$6,000.00
Clark Company	3,000.00
Interest	6,292.00
Income from partnerships: Megathlin and Clark	100.99
Rent	400.00
Other income:	
First-mortgage bonds, Clark Company, in payment of interest	20,500.00
Second-mortgage bonds, Clark Company, in payment of losses sustained as endorser on notes of the Bowers Company and deducted as bad debts in prior years	58,000.00

In addition to the loss of $92,500 sustained on the sale of Bowers Company stock the petitioner reported losses of $5,215.02 and $178.45 from the partnerships of D. M. Picton and Company and the Florida Dredging Company. He also took deductions of $1,360 and $24.70 for interest and taxes, respectively, making a net loss reported of $4,985.18. No deduction was taken on the 1922 return for the net loss for 1921 or any part of it.

For 1923 the petitioner reported a total net income of $24,727.82, which the respondent in determining the deficiency for that year increased to $43,037.93. The petitioner took as a deduction in his 1923 return the 1922 net loss of $4,985.10, but this was disallowed by the respondent. While the petitioner did not take any deduction in his 1923 return on account of the net loss for 1921, he requested allowance of such deduction prior to the final determination of his

tax liability for 1923. The respondent in determining the deficiency did not allow the deduction.

In his return for 1925 the petitioner took a deduction of $1,850 as a loss sustained on the exchange of an old auto for a new one. In determining the deficiency for 1925 the respondent disallowed the deduction. The petitioner is entitled to $950 of the deduction taken.

Opinion

TRAMMELL: Counsel for the respondent admitted at the hearing that the petitioner is entitled to a deduction of $950 as a loss sustained on the exchange of an automobile. This loss should, therefore, be allowed.

The remaining issue involves the consideration of two matters, namely, whether the loss of $68,000 resulting from the petitioner's payment in 1921 of notes of the Bowers Company, on which he was endorser, and the losses resulting in 1921 and 1922 from the sale of the stock owned by him in the Bowers Company constitute net losses within the meaning of the term as used in the act.

16 Section 204 of the revenue act of 1921 provides in part as follows:

" (a) That as used in this section the term " net loss " means only net losses resulting from the operation of any trade or business regularly carried on by the taxpayer (including losses sustained from the sale or other disposition of real estate, machinery, and other capital assets used in the conduct of such trade or business); * * *

" (b) If for any taxable year beginning after December 31, 1920, it appears upon the production of evidence satisfactory to the commissioner that any taxpayer has sustained a net loss, the amount thereof shall be deducted from the net income of the taxpayer for the succeeding taxable year; and if such net loss is in excess of the net income for such succeeding taxable year, the amount of such excess shall be allowed as a deduction in computing the net income for the next succeeding taxable year; the deduction in all cases to be made under regulations prescribed by the commissioner with the approval of the Secretary."

The petitioner contends that the losses here involved were losses resulting from the operation and conduct of a trade or business regularly carried on by him and that the excess thereof over the income for 1921 and 1922 is deductible in determining taxable income for 1923.

In order for the losses here involved to be deductible in determining taxable income for 1923, they must be net losses resulting from the operation of a trade or business regularly carried on by the petitioner and not from isolated and occasional transactions. (J. J. Harrington, 1 B. T. A. 11; Oscar E. Rehm, 16 B. T. A. 1045.)

With respect to the loss of $68,000 resulting from the petitioner's endorsement of the Bowers Company notes, he testified that in en-

dorsing the notes he was seeking to protect his investment in its stock. Aside from endorsing an undisclosed number of notes of this company there is nothing in the record to indicate that acting as endorser or guarantor constituted a business or trade with the petitioner. So far as the record shows these were the only notes ever endorsed by the petitioner for the Bowers Company or for any other company or person. From the facts in the case we are
17 of the opinion that the loss did not result from the operation of a trade or business regularly carried on by the petitioner but resulted from isolated or occasional transactions. The petitioner's contention as to this item is denied. (See Edward Hines, 18 B. T. A. 21, and Wm. J. Robb, 5 B. T. A. 827.)

With respect to the remaining losses resulting from the sale of the Bowers Company stock in 1921 and 1922, we do not think the petitioner's ownership of stock in a number of corporations which he held as an investment during 1921 and 1922 or the sale or some of such stock in those years constituted a business or trade regularly carried on by him. As to his being in the investment business, the petitioner testified as follows:

"Q. Would you say you were in the investment business, Mr. Clark?—A. No, sir."

Since the petitioner was not in the investment business or engaged in the business of a dealer in securities, we think the losses resulting from the sale of the Bowers Company stock in 1921 and 1922 constituted losses arising from occasional or isolated transactions and not from the operation of a business regularly carried on. The petitioner's contention as to them must also be denied. (J. L. Washburn, 16 B. T. A. 1091; Oscar E. Rehm, supra.)

Judgment will be entered under rule 50.

Now, March 18, 1931, the foregoing findings of fact and opinion certified from the record as a true copy.

[Seal, U. S. Board of Tax Appeals.]

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

Before United States Board of Tax Appeals, Washington

Docket No. 34824

R. P. CLARK, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Decision

Pursuant to opinion and findings of fact promulgated May 5, 1930, the respondent herein, to wit, on August 21,
18 1930, having filed a proposed redetermination for the years 1923 and 1925, and the petitioner on August 27, 1930, hav-

ing filed notice of acquiescence to the said proposed redetermination, it is

Ordered and decided that there are deficiencies for the years 1923 and 1925 in the amounts of $2,722.41 and $311.73, respectively.

Enter.

(Signed) CHARLES M. TRAMMELL,
Member.

Entered Aug. 29, 1930.

vlh.

A true copy. Teste:

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

Now, March 18, 1931, the foregoing decision certified from the record as a true copy.

[Seal, U. S. Board of Tax Appeals.]

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

Before United States Board of Tax Appeals

[Title omitted.]

Stipulation of venue

Filed Feb. 21, 1931

It is hereby stipulated and agreed by and between the respective parties hereto, acting by their respective counsel, that the Court of Appeals of the District of Columbia may take jurisdiction of the petition for review in the above-entitled cause and may review the decision of the Board of Tax Appeals entered therein. This
19 stipulation is made and entered into under and pursuant to subdivision (d) of section 1002 of the revenue act of 1926.

WM. S. HAMMERS,
Attorney for Petitioner.
C. M. CHAREST,
General Counsel, Bureau of Internal Revenue, for the Respondent.

Now, March 18, 1931, the foregoing stipulation of venue certified from the record as a true copy.

[Seal, U. S. Board of Tax Appeals.]

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

In Court of Appeals of the District of Columbia

[Title omitted.]

Petition for review of decision of United States Board of Tax Appeals

Filed Feb. 26, 1931

To the honorable Judges of the Court of Appeals of the District of Columbia:

Your petitioner, R. P. Clark, in support of this his petition, filed in pursuance of the provisions of section 1001 of the act of Congress approved February 26, 1926, entitled the "Revenue Act of 1926," for review of the decision of the United States Board of Tax Appeals, promulgated May 5, 1930, and the order of the board entered herein on August 29, 1930, approving a deficiency in income and profits tax of petitioner for the calendar year 1923, in the amount of $2,722.41, respectfully shows to this honorable court as follows:

I

STATEMENT OF THE NATURE OF THE CONTROVERSY

1. The controversy relates to the income and profits tax of petitioner for the calendar year 1923, and the deductibility in that year of net losses of $17,768.51 and $4,985.18 sustained by petitioner in the years 1921 and 1922, respectively, claimed to have been net losses resulting from the operation of his trade or business regularly carried on, within the meaning of section 204 (a) and (b) of the revenue act of 1921 and deductible in 1923.

Petitioner, who is a resident of Miami, Florida, has been engaged since 1888 in the business of river and harbor work, dredging, and jetty-building operations. He was associated with the Bowers Southern Dredging Company from the time of its organization in Texas in 1899 until the company was taken over by the Clark Dredging Company in 1922. Petitioner became president of the Bowers Company in 1905 and continued in that capacity as long as it continued to operate, and he was the active directing head of the corporation. During 1921 and in 1922 until the business was taken over by the Clark Company petitioner, who was the majority stockholder, was the managing operator of the Bowers Company for a committee of its creditors. In addition to his association with the Bowers Company, which was engaged in dredging and other river, harbor, and jetty work, petitioner owned a partnership interest and took active part in the affairs of D. M. Picton and Company, Port Arthur, Texas, the Florida Dredging Company, Miami, Florida, and Megathlin & Clark, Miami, Florida, all of which

were likewise engaged in dredging, jetty building, and river improvement work.

When the Bowers Southern Dredging Company was organized in 1899, the original capitalization was $600,000, divided into shares of a par value of $100 each, and petitioner owned 1,800 shares, which he received for assets turned over to the corporation. In 1910 the company's capital stock was increased to $750,000, the additional stock being sold at par for cash. By 1922 petitioner's stock holdings in the company had increased to more than 3,000 shares, the additional shares having been acquired by him from time to time, some as late as 1914, for all of which he paid the full par value of $100 a share. Up to 1917 the company paid dividends regularly and from 1907 to 1917 its stock had a value in excess of par.

In 1917, when the war started, the Bowers Southern Dredging Company had many contracts on hand to complete and began to have financial difficulties, which brought its affairs in 1921 into the hands of a creditors' committee. The company was unable to borrow money from the banks with which to operate its business without the individual indorsement of petitioner on its notes. In 1921 petitioner was required to pay $68,000 on notes of the company which he had endorsed from time to time in the regular course of business, and this amount he deducted as a loss in his tax return for 1921. Petitioner also sold in 1921, 100 shares of his stock in the Bowers Southern Dredging Company in order to raise $500 which he needed badly at the time and reported in his return for 1921 a loss from sale of said stock of $9,500. The total net loss sustained by petitioner in 1921, and reported in his return, was $17,768.51, which was allowed by the Commissioner of Internal Revenue in the final audit of the return.

In 1922, petitioner sold 1,000 shares of his stock in the Bowers Southern Dredging Company to one George H. Nolan, whom he desired to have become associated with the company to improve its standing, for the sum of $7,500, and in his return for 1922 he accordingly took as a deduction a loss of $92,500 sustained on the sale of the stock, which represented the difference between its cost of $100,000 and the selling price. There was also an operating loss of $5,215.02 which petitioner sustained in the partnership of D. M. Picton & Company, and a similar loss of $178.45 sustained in the Florida Dredging Company. The total net loss reported by petitioner in his return for 1922 was $4,985.18, which was approved by the Commissioner of Internal Revenue in the final audit of the return.

2. For 1923 the petitioner took as a deduction in his return the 1922 net loss of $4,985.18 as resulting from the operation of his trade
22 or business regularly carried on by him, as provided in section 204 (a) and (b) of the revenue act of 1921; but this deduction was disallowed by the Commissioner of Internal Revenue. Furthermore, while the petitioner did not take any deduction in his 1923

return on account of the net loss for 1921 of $17,768.51 as a net loss also resulting from the operation of his trade or business, he requested allowance of such deduction prior to the final determination of his tax liability for 1923, but the Commissioner of Internal Revenue in determining the deficiency of $2,722.41 for that year likewise refused to allow this deduction.

3. From the determination of the Commissioner of Internal Revenue asserting a deficiency in tax for the year 1923 as a result of the disallowance of the claimed deductions of the net losses for 1921 and 1922, an appeal was seasonably taken to the United States Board of Tax Appeals. In the proceeding before the board the petitioner contended that the losses sustained by him from his indorsement of the Bowers Southern Dredging Company's notes in 1921, and also from the sale of that company's stock in 1921 and 1922, resulted from the operation of a trade or business regularly carried on by him within the meaning of section 204 (a) and (b) of the revenue act of 1921, and that therefore the respondent, in determining the tax liability for 1923, erred in not allowing as deductible items the net loss for 1922 of $4,985.18, which petitioner had carried forward and deducted on his return for 1923, and the net loss of $17,768.51, sustained in 1921, which he had not so forwarded and deducted in his 1923 return, but which, he claimed, was an allowable deduction and should have been allowed. Upon hearing and consideration of petitioner's appeal the board decided that said losses to petitioner in 1921 and 1922 did not result from the operation of a trade or business regularly carried on by petitioner but resulted from isolated or occasional transactions, that the petitioner's contentions must be denied, and that judgment should be entered for the commissioner as respondent. An order was accordingly entered by said board on August 29, 1930, determining a deficiency of $2,722.41 for the year 1923.

23

II

DESIGNATION OF COURT OF REVIEW

Your petitioner, being aggrieved by the decision of the board promulgated May 5, 1930, and the order of redetermination entered August 29, 1930, in the proceeding before the board designated as Docket No. 34824, respectfully submits this his petition for a review thereof by the Court of Appeals of the District of Columbia, in accordance with the stipulation between the parties filed with the board pursuant to the provisions of section 1002 (d) of the revenue act of 1926.

III

ASSIGNMENTS OF ERRORS

Your petitioner believes and avers that errors were committed by the board, to his damage and prejudice, and as a basis for review sets forth the following:

1. The Board of Tax Appeals erred in holding as a matter of law that in determining petitioner's net income for 1923 there could not be allowed as a proper deduction, as provided for in section 204 (b) of the revenue act of 1921, a net loss sustained by the petitioner for the calendar year 1921 amounting to $17,768.51 in excess of any taxable income for 1922.

2. The board erred in holding as a matter of law that in determining the taxable net income of petitioner for the year 1923 there could not be allowed as a proper deduction from the net income, as provided in section 204 (a) and (b) of the revenue act of 1921, the loss sustained by petitioner for the calendar year 1922, which net loss amounted to $4,985.18.

3. The board erred in holding as a matter of law that petitioner's net losses for the years 1921 and 1922 in the amounts of $17,768.51 and $4,985.18, respectively, were not net losses resulting from the operation of a trade or business regularly carried on by petitioner within the meaning of section 204 (a) and (b) of the revenue act of 1921, and therefore not proper deductions in determining the tax liability of petitioner for the year 1923.

24 4. The board erred in holding as a matter of law that a loss of $68,000 resulting from the petitioner's payment in 1921 of notes of the Bowers Southern Dredging Company, on which he was indorser, and also the losses of $9,500 and $92,500 in 1921 and 1922, respectively, resulting from the sale of stock owned by petitioner in the Bowers Southern Dredging Company, were not losses resulting from the operation of a trade or business regularly carried on by petitioner, within the meaning of section 204 (a) and (b) of the revenue act of 1921, and that the excess of said losses over the income for the respective years 1921 and 1922 was not deductible in determining taxable income of petitioner for the year 1923.

5. The board erred in rendering decision for the respondent.

6. The board erred in rendering judgment for a deficiency of $2,722.41 for the calendar year 1923 against petitioner.

Wherefore your petitioner prays that the decision and order of the Board of Tax Appeals, relative to the deficiency in tax for the year 1923, entered herein against it, be reviewed and reversed by this honorable court, and that the clerk of the board be directed to transfer and deliver to the clerk of this court certified copies of all and every of the documents necessary and material to the presentation and consideration of the foregoing petition for review and as required by the statutes and rules of said court made and provided.

R. P. CLARK,
By WM. S. HAMMERS,
501 Union Trust Bldg., Washington, D. C.,
Attorney for Petitioner.

[*Duly sworn to by Wm. S. Hammers; jurat omitted in printing.*]

25 Now, March 18, 1931, the foregoing petition for review certified from the record as a true copy.

[Seal, U. S. Board of Tax Appeals.]

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

Before United States Board of Tax Appeals

[Title omitted.]

Præcipe for transcript of record

Filed Feb. 26, 1931

To the Clerk of the United States Board of Tax Appeals:

You will please prepare and, within 60 days from the date of the filing of the petition for review in the above-entitled case, transmit to the clerk of the Court of Appeals of the District of Columbia copies of the following documents:

1. The docket entries of proceedings before the board.
2. Pleadings before the board.
3. Findings of fact, opinion, and decision of the board, and its order of redetermination.
4. Petition for review.
5. Stipulation that the Court of Appeals of the District of Columbia may take jurisdiction of petition for review.
6. This præcipe.

26 The foregoing to be prepared, certified, and transmitted as required by law under the rules of the Court of Appeals of the District of Columbia.

WM. S. HAMMERS,
Attorney for Petitioner.

Now, March 18, 1931, the foregoing præcipe certified from the record as a true copy.

[Seal, U. S. Board of Tax Appeals.]

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

[Endorsed on cover:] Board of Tax appeals. No. 5386. R. P. Clark, appellant, vs. David Burnet, Commissioner of Internal Revenue. Court of Appeals, District of Columbia. Filed Apr. 13, 1931. Henry W. Hodges, clerk.

(628)

27 [Minute entries of argument and submission, March 10th and 11th, 1932, omitted in printing.]

28 [Omitted.]

29 In Court of Appeals of the District of Columbia

No. 5386

R. P. CLARK, APPELLANT

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

Appeal from the Board of Tax Appeals

Argued March 10, 1932. Decided April 11, 1932

Wm. S. Hammers, of Washington, D. C., for appellant.

G. A. Youngquist, Sewall Key, C. M. Charest, Frank M. Thompson, jr., and S. Dee Hanson, all of Washington, D. C., for appellee.

Before Martin, Chief Justice, and Robb, Van Orsdel, and Groner, Associate Justices.

Opinion

MARTIN, Chief Justice: An appeal from a decision of the Board of Tax Appeals denying certain deductions claimed by taxpayer under section 204 (a) of the revenue act of 1921, as net losses resulting from the operation during the taxable year of a trade or business regularly carried on by taxpayer.

The record discloses that since 1888 appellant was engaged in the business of dredging and supervising dredging operations off the coast of Florida and elsewhere. From 1899 he was associated with the Bowers Southern Dredging Company, hereinafter called the Bowers Company. He was its majority stockholder, its active directing head, and devoted all of his time to its operation.

In addition to his association with the Bowers Company appellant in 1921 and 1922 was a member of the partnerships of D. M. Picton & Company, Port Arthur, Texas, the Florida Dredging Company, Miami, Florida, and Megathlin & Clark, Miami, Florida. Megathlin & Clark and the Florida Dredging Company were engaged in the dredging business and D. M. Picton & Company was engaged in river and harbor work and jetty building. Appellant took an active advisory interest in these partnerships whose work was mostly in connection with the work of the Bowers Company. In 1921 and 1922 appellant also owned stock in a number of corporations which he held as investments.

30 At the beginning of the war in 1917 the Bowers Company had many contracts to complete and began to experience financial difficulties. This finally resulted in its business being placed in the hands of a creditors' committee under which it was operated in 1921. During this time appellant served as managing operator of the company for the creditors. The company was unable to borrow money from banks without the individual indorsement of appellant,

therefore in order to protect his investment in the company appellant at various times became indorser upon notes of the company. In 1921 as a result of such indorsements appellant was forced to pay the sum of $68,000 for the company. This amount he took as a deduction for losses in his 1921 income-tax return and it was allowed by the commissioner.

In his return for 1921 appellant also reported a loss of $9,500 incurred by him in a sale of the Bowers Company stock. The loss was allowed by the commissioner in the final audit of the return.

In 1922 appellant being desirous of having some one with financial strength associated with the business of the Bowers Company, sold 1,000 shares of the stock owned by him in the company, which he had purchased at a cost of $100,000, to George H. Nolan for $7,500. In his return for 1922 appellant accordingly took a deduction for the loss thus sustained in the amount of $92,500, which represented the difference between the cost and selling price of the stock. In the final audit of the return this loss was allowed by the commissioner.

However, appellant's income for the years 1921 and 1922, respectively, was not sufficient to absorb the net losses thus suffered by appellant in those years, but left a net loss of $17,768.51 in 1921 and $4,985.18 in 1922, and appellant claimed the right to deduct these sums from his income-tax returns in the succeeding years, as net "business losses" coming within the provisions of section 204, supra. This claim was disallowed by the commissioner, and his decision was affirmed by the Board of Tax Appeals. (19 B. T. A. 859.)

Section 204, supra, reads in part as follows:

"(a) That as used in this section the term 'net loss' means only net losses resulting from the operation of any trade or business regularly carried on by the taxpayer * * *.

"(b) If for any taxable year beginning after December 31, 1920, it appears upon the production of evidence satisfactory to the commissioner that any taxpayer has sustained a net loss, the amount thereof shall be deducted from the net income of the taxpayer for the succeeding taxable year; and if such net loss is in excess of the net income for such succeeding taxable year, the amount of such excess shall be allowed as a deduction in computing the net income for the next succeeding taxable year; * * *."

It may be observed that no question is made in this case as to the amounts, dates, or actual circumstances of appellant's losses, and that the sole issue is whether they are within the purview of the foregoing statute.

The Board of Tax Appeals placed its decision upon the ground that the losses resulting from appellant's indorsement of the company's notes, as well as those resulting from the sale of company stock, did not result from the operation of any trade or
31 business regularly carried on by appellant, but only from "isolated or occasional transactions."

We do not agree with this conclusion.

It appears that during the times in question appellant was engaged in regularly carrying on the business of dredging, operated by a corporation of which appellant was principal owner and active directing head, and to which he devoted all of his time and energies. Appellant accordingly was necessarily concerned with the financial conditions and difficulties which beset the business, and he was compelled by circumstances to indorse the company's notes in order to supply it with necessary operating funds. This action was not isolated or occasional but became part of the operation of the business, and helped to carry it on. It is true that appellant did not regularly carry on a business of indorsing notes for profit, but his indorsement of the company's notes was part of the business regularly carried on for the company. It is also true that appellant was not regularly engaged in the business of selling corporate stocks, but the transactions of that character appearing in the record can not be separated from the regular course of business of which they were part, and must not be considered as if wholly independent transactions.

The decision of the board in the present case, moreover, does not seem consistent with its decisions in similar cases of more recent date.

In the case of E. D. Anthony (20 B. T. A. 5) the taxpayer was engaged in the retail shoe business, first as a member of a partnership, then as stockholder of a corporation which took over the business. The business suffered reverses, and taxpayer sold preferred stock to friends, loaned stock to be used as collateral for the company's loans, and paid $20,000 upon its indebtedness. The corporation was afterwards liquidated and taxpayer in 1923 sustained a heavy loss on the stock he owned in it. The board held that this loss was deductible as a net business loss in computing taxpayer's net income for 1924.

In Glenn M. Averill (20 B. T. A. 1196, 1198) the board, referring to similar losses, said: "On the other hand, upon the sale of such stock or bond or upon the failure or liquidation of the corporation the stockholder or bondholder may sustain an operating loss. This is entirely different from the operating loss of the corporation, and must rest upon the ground that investments in such stocks or bonds is a part of, or incident to, the operation of a trade or business regularly carried on by the taxpayer. It is obvious that an individual may suffer a 'net loss' within the meaning of the statute upon the failure of a corporation or a sale or other disposition of his interest therein."

In Heller v. Commissioner (25 B. T. A. 259) the petitioners were stockholders in and managed and operated the business of several corporations engaged in retailing ladies' ready-to-wear clothing; and the board held that a loss resulting from the sale of stock in one of such corporations was a loss sustained in carrying on a business and the amount thereof should be included in computing a "net loss" under section 206 (a) (1) of the revenue act of 1926.

32 In Washburn v. Commissioner of Internal Revenue (C. C. A.) (51 F. (2d) 949) it was held, "Where attorney organized and invested in corporation, and devoted most of his time to management thereof, loss sustained on sale of stock in corporation was loss occurring in 'business' regularly carried on and deductible from income of next succeeding year. (Revenue act of 1921, sec. 204 (a) and (b).)"

The commissioner cites among others the case of Goldberg v. Commissioner (36 F. (2d) 551), where the taxpayer sustained losses in an individual real-estate transaction, which he later transferred to his real-estate corporation; also Pabst v. Lucas (36 F. (2d) 614) where the taxpayer sustained losses in investments wholly foreign to his regular business. In both cases deductions claimed under section 204, supra, were rightly disallowed. These decisions, however, do not serve as authority here. The commissioner cites also Anderson v. United States (C. C. A.) (48 F. (2d) 201) wherein such a deduction was disallowed to a taxpayer who is said to have been "interested" in certain business enterprises without finding, however, that the business had been regularly carried on by him. The decision as reported is not inconsistent with our conclusion in the present case. Other authorities cited by the commissioner have been examined by us, but they do not require specific mention here.

Upon the grounds stated we reverse the decision of the Board of Tax Appeals, and the case is remanded for further action not inconsistent with this opinion.

A true copy. Teste:

_____, _____,

Clerk, Court of Appeals, D. C.

33 In Court of Appeals of District of Columbia

No. 5386, April Term, 1932

R. P. CLARK, APPELLANT

vs.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

Judgment

April 11, 1932

Appeal from the Board of Tax Appeals. This cause came on to be heard on the transcript of the record from the Board of Tax Appeals and was argued by counsel. On consideration whereof, it is now here ordered, adjudged, and decreed by this court that the decision of the said Board of Tax Appeals in this cause be, and the same is hereby, reversed and that this cause be, and the same is

hereby, remanded to the said Board of Tax Appeals for further action not inconsistent with the opinion of this court.

Per Mr. Chief Justice MARTIN.

APRIL 11, 1932.

Mr. Justice Hitz took no part in the consideration or decision of this case.

34 In Court of Appeals of the District of Columbia

[Title omitted.]

Præcipe for transcript of record

Filed June 10, 1932

The clerk, in preparation of the transcript of the record on petition for certiorari to the Supreme Court of the United States, shall include the following:

1. The transcript of record.
2. Argument.
3. Decision.
4. Opinion of the court.
5. This designation.
6. Clerk's certificate.

T. D. THACHER,
Solicitor General.

[File endorsement omitted.]

35 [Clerk's certificate to foregoing transcript omitted in printing.]

36 Supreme Court of the United States

Order allowing certiorari

Filed October 10, 1932

The petition herein for a writ of certiorari to the Court of Appeals of the District of Columbia is granted, and the case is assigned for argument immediately following case No. 95, Burnet, Commissioner of Internal Revenue, vs. Commonwealth Improvement Co.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[Endorsed on cover:] File No. 36877. District of Columbia, Court of Appeals. Term No. 180. David Burnet, Commissioner of Internal Revenue, petitioner, vs. R. P. Clark. Petition for a writ of certiorari and exhibit thereto. Filed June 27, 1932. File No. 36877.

U. S. GOVERNMENT PRINTING OFFICE: 1932

FILE COPY

Office Supreme Court, U. S.
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JUN 27 1932
CHARLES ELMORE CROPLEY
CLERK

No. 180

In the Supreme Court of the United States

OCTOBER TERM, 1932

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

R. P. CLARK

PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE DISTRICT OF COLUMBIA

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126323—32

In the Supreme Court of the United States

OCTOBER TERM, 1932

No. ——

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

R. P. CLARK

PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE DISTRICT OF COLUMBIA

The Solicitor General, on behalf of the Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the Court of Appeals of the District of Columbia entered in the above cause on April 11, 1932, reversing the judgment of the Board of Tax Appeals.

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 15–17) is reported in 19 B. T. A. 859. The opinion of the Court of Appeals (R. 27) is not yet reported.

JURISDICTION

The judgment of the Court of Appeals was entered April 11, 1932. The jurisdiction of this

Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether, under the circumstances of this case, the losses sustained in 1921 by respondent by reason of the payment of certain notes of the Bowers Southern Dredging Company which he had endorsed, and in 1921 and 1922 from the sale of certain stock of that corporation, constituted "net losses resulting from the operation of any trade or business regularly carried on by the taxpayer" within the meaning of Section 204 (a) of the Revenue Act of 1921.

STATUTE AND REGULATIONS INVOLVED

The applicable statute and regulations are set forth in the Appendix, *infra*, pp. 9–11.

STATEMENT

The pertinent facts, as found by the Board of Tax Appeals (R. 10–15), may be summarized as follows:

Since 1888 respondent, R. P. Clark, has been engaged in the business of dredging and supervising dredging operations. He was associated with the Bowers Southern Dredging Company from the date of its organization in 1899 until September, 1922. That company was engaged in dredging and other river, harbor, and jetty work. Respondent became president and active directing head of the

Bowers Company in 1905 and so continued and devoted all of his time to its operation during that time. In September, 1922, respondent became president of the Clark Dredging Company which was then organized and took over the business of the Bowers Company. (R. 11–12.)

In 1921 and 1922 respondent owned, as investments, stock in a number of corporations, and in addition to his activities in the Bowers Company, was a member of and took an active advisory interest in three partnerships. The partnerships were engaged in the business of dredging, river and harbor work, and jetty building, mostly in connection with the work of the Bowers Company. (R. 12.)

At the beginning of the war in 1917, the Bowers Company had many contracts to complete and began to experience financial difficulties. This finally resulted in its business being placed in the hands of a creditors' committee under which it was operated in 1921. During this time respondent, majority stockholder in the Bowers Company, served as managing operator of the company for the creditors' committee and continued as such until the Clark Company succeeded to the business in 1922. The Bowers Company was unable to borrow money from banks without the individual indorsement of respondent. Therefore, in order to protect his investment in the company, respondent at various times became indorser upon notes of the

company. In 1921, as a result of such indorsements, respondent was forced to pay the sum of $68,000 for the company. This amount, together with a loss of $9,500 suffered by him in the sale of the Bowers Company stock in 1921, respondent took as a deduction for losses on his 1921 income-tax return, and the deduction was allowed by the Commissioner in the final audit of the return. (R. 12–13.)

In 1922 respondent, being desirous of having some one with financial strength associated with the business of the Bowers Company, sold 1,000 shares of the stock owned by him in the company, which he had purchased at a cost of $100,000, to George H. Nolan for $7,500. In his return for 1922 respondent accordingly took a deduction for the loss thus sustained in the amount of $92,500, which represented the difference between the cost and selling price of the stock. In the final audit of the return this loss was allowed by the Commissioner. (R. 14–15.)

Respondent's income for 1921 and 1922 was not sufficient to absorb the losses sustained in those years but left remaining unabsorbed net losses of $17,768.51 in 1921 (R. 13), and $4,985.10 in 1922 (R. 15). Respondent claimed the right, under Section 204 of the Revenue Act of 1921, *infra*, p. 9, to carry these sums forward and deduct them in his tax returns for succeeding taxable years as "net losses resulting from the operation of any

trade or business regularly carried on by the taxpayer." The Commissioner disallowed deduction on respondent's 1923 return of the "net losses" thus claimed. (R. 6–9.) The Board of Tax Appeals sustained the Commissioner's determination on the ground that the losses resulted from isolated or occasional transactions. (R. 10–11, 16–17.)

The taxpayer, under stipulation entered into pursuant to Section 1002 (d) of the 1926 Revenue Act, filed his petition for review in the Court of Appeals of the District of Columbia (R. 18–19), which reversed the decision of the Board of Tax Appeals.

SPECIFICATION OF ERRORS TO BE URGED

The Court of Appeals of the District of Columbia erred:

1. In holding that the losses sustained by ~~petitioner~~ respondent were "net losses resulting from the operation of any trade or business regularly carried on by the taxpayer" within the meaning of Section 204 (a) of the Revenue Act of 1921.

2. In reversing the decision of the Board of Tax Appeals.

REASONS FOR GRANTING THE WRIT

1. The decision of the court below, citing with approval *Washburn* v. *Commissioner,* 51 F. (2d) 949 (C. C. A. 8th), is in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *Dalton* v. *Bowers,* 56 F. (2d) 16 (C. C.

A. 2d). We did not oppose the petition in the *Dalton* case beause of the apparent conflict between the decision in that case and the decisions in the *Washburn* case and the instant case and because of the importance of the question. Certiorari was granted on May 31, 1932 (No. 52, October Term, 1932).

In the *Dalton* case, the taxpayer, an inventor and engineer, had organized the Dalton Manufacturing Company, a New York corporation, of which he became the president, treasurer, and a director. He owned all the capital stock, which cost him $395,000, and made unsuccessful efforts to sell the stock to the public. He devoted his time to inventing. The Dalton Manufacturing Company was employed in manufacturing and marketing articles of his invention. He was in active charge of the company and its affairs, and from its incorporation until September, 1924, spent the greater part of his time at its office, receiving no compensation for his labors, although he was credited with a salary from 1917 to 1922, inclusive. In December, 1923, the liabilities exceeded the assets by $173,462, and in that year it ceased operations and took steps to wind up its business. Its assets were sold during 1924. The profits of the sale were insufficient to pay its creditors. However, the taxpayer advanced sufficient funds to the corporation for that purpose and he had earlier advanced other sums to it. It was not actually dissolved until 1925, when the taxpayer surrendered his stock for cancellation. In his re-

turn for 1925 he claimed a deduction for the loss sustained in 1924 when his investment in the stock of the corporation became worthless, pursuant to Section 206 (a) and (b) of the Revenue Act of 1924, as a loss "attributable to the operation of a trade or business regularly carried on by the taxpayer." The Circuit Court of Appeals, reversing the judgment of the District Court, held that the Dalton Manufacturing Corporation was a legal entity, separate and distinct from Dalton, its stockholder, and that inasmuch as Dalton chose to do business through the corporation, his loss was a capital loss and did not occur in the operation of a trade or business regularly carried on by him. Despite the differences in fact, the application of the same principles to this case and the *Dalton* case would doubtless have changed the result in one of the two cases.

The decision of the court below appears also to be in conflict with the principles applied in *Anderson* v. *United States* 48 F. (2d) 201 (C. C. A. 5th); *Eli Strouse* v. *Commissioner* (C. C. A. 4th), decided June 13, 1932, not yet reported; *Hughes* v. *Commissioner,* 38 F. (2d) 755 (C. C. A. 10th); *Goldberg* v. *Commissioner,* 36 F. (2d) 551 (App. D. C.); and *Pabst* v. *Lucas,* 36 F. (2d) 614 (App. D. C.).

2. For the reasons stated in the memorandum submitted on behalf of the Government in the *Dalton* case, the question whether losses incurred as a

creditor or a stockholder of a corporation by a taxpayer who is actively engaged in the management of an incorporated enterprise are deductible "net losses" under the applicable Revenue Acts is of general importance. We believe that the decision of the court below in this case was erroneous. In order to preserve the rights of the Government pending the consideration of the question in the *Dalton* case, it is respectfully submitted that the present petition should be granted.

In the event that this Court grants the petition, it is suggested that this case be assigned for argument immediately after the *Dalton* case.

THOMAS D. THACHER,
Solicitor General.

JUNE, 1932.

APPENDIX

STATUTE AND REGULATIONS INVOLVED

REVENUE ACT OF 1921 C. 136, 42 STAT. 227, 231

SEC. 204. (a) That as used in this section the term "net loss" means only net losses resulting from the operation of any trade or business regularly carried on by the taxpayer (including losses sustained from the sale or other disposition of real estate, machinery, and other capital assets, used in the conduct of such trade or business); and when so resulting means the excess of the deductions allowed by section 214 or 234, as the case may be, over the sum of the following: (1) The gross income of the taxpayer for the taxable year, (2) the amount by which the interest received free from taxation under this title exceeds so much of the interest paid or accrued within the taxable year on indebtedness as is not permitted to be deducted by paragraph (2) of subdivision (a) of section 214 or by paragraph (2) of subdivision (a) of section 234, (3) the amount by which the deductible losses not sustained in such trade or business exceed the taxable gains or profits not derived from such trade or business, (4) amounts received as dividends and allowed as a deduction under paragraph (6) of subdivision (a) of section 234, and (5) so much of the depletion deduction allowed with respect to any mine, oil or gas well as is based upon discovery value in lieu of cost.

(b) If for any taxable year beginning after December 31, 1920, it appears upon the production of evidence satisfactory to the Commissioner that any taxpayer has sustained a net loss, the amount thereof shall be deducted from the net income of the taxpayer for the succeeding taxable year; and if such net loss is in excess of the net income for such succeeding taxable year, the amount of such excess shall be allowed as a deduction in computing the net income for the next succeeding taxable year; the deduction in all cases to be made under regulations prescribed by the Commissioner with the approval of the Secretary.

TREASURY REGULATIONS 62

ART. 1601. *Net losses, definition and computation.*—The term "net loss" as used in the statute means only a net loss resulting from the operation during the taxable year of any trade or business regularly carried on by the taxpayer. Included therein are losses from the sale or other disposition of real estate, machinery, and other capital assets used in the conduct of such trade or business. In order to be entitled to claim an allowance for a "net loss" the taxpayer must have suffered an actual net loss in a trade or business during the taxable year. The amount properly allowable may be neither the loss reflected upon the return filed for the purpose of the income tax nor the net loss shown by the taxpayer's profit and loss account, but is to be computed according to the statute, as follows:

(1) In the case of an individual, it is the amount by which the deductions allowed under section 214, excluding:

(a) the amount by which the deductible losses not sustained in such trade or business exceed the taxable gain or profits not derived from such trade or business;

* * * * *

(c) the amount of deductions allowed under section 214 not connected with the trade or business,

exceeds the sum of the following:

(a) the gross income of the taxpayer for the taxable year as computed under section 213; and

(b) the amount by which the interest received free from taxation under the provisions of the Act exceeds so much of the interest paid or accrued within the taxable year on indebtedness as is not allowed as a deduction under section 214 (a) (2).

* * * * *

In computing statutory "net loss" the following restrictions are to be noted:

(1) Interest received by the taxpayer on obligations or securities, the interest from which is exempted from taxation must be included in income, but this amount may first be reduced by the amount of any interest paid by the taxpayer on money used to purchase or carry such obligations or securities.

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CHARLES ELMORE

No. 180

In the Supreme Court of the United States

OCTOBER TERM, 1932

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

R. P. CLARK

ON A WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE DISTRICT OF COLUMBIA

BRIEF FOR THE PETITIONER

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In the Supreme Court of the United States

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No. 180

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

R. P. CLARK

ON A WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE DISTRICT OF COLUMBIA

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 11–12) is reported in 19 B. T. A. 859. The opinion of the Court of Appeals of the District of Columbia is reported in 59 F. (2d) 1031. (R. 19.)

JURISDICTION

The judgment of the Court of Appeals was entered April 11, 1932. (R. 22.) Petition for a writ of certiorari was filed June 27, 1932, and granted October 10, 1932. (R. 23.) Jurisdiction is

conferred upon this Court by Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Were the losses sustained by respondent in 1921 by reason of his indorsement and payment of certain notes of the Bowers Southern Dredging Company and in 1921 and 1922 from the sale of certain stock of that corporation "net losses resulting from the operation of any trade or business regularly carried on by the taxpayers," within the meaning of Section 204 (a) of the Revenue Act of 1921?

STATUTE AND REGULATIONS INVOLVED

These are set forth in the Appendix, *infra*, pp. 9–11.

STATEMENT

The findings of fact made by the Board of Tax Appeals (R. 7–11) may be summarized as follows:

Bowers Southern Dredging Company (hereinafter referred to as the Bowers Company) was organized in 1899 (R. 8), and between that time and September 1, 1922 (R. 10), was engaged in dredging and other river, harbor, and jetty works (R. 8). At the time of its organization respondent became a stockholder (R. 8) and associated with the company (R. 8). In 1905 he became its president, and remained in that capacity as long as the company continued to operate. As president and majority stockholder he was the active direct-

ing head of the corporation, devoting all of his time to its operations. (R. 8.)

At the beginning of the war in 1917 the company began to experience financial difficulties. This finally resulted in its business being placed in the hands of a creditors' committee, under which it was operated in 1921 (R. 9) and until September 1, 1922 (R. 8), when the Clark Dredging Company, organized by respondent, took over its assets and liabilities (R. 10). During the time that the business of the Bowers Company was in the hands of the creditors' committee respondent served as managing operator of the company for that committee, and continued as such until September 1, 1922. (R. 8.)

The Bowers Company was unable to borrow money from banks without the individual indorsement of respondent, and therefore at various times, in order to protect his investment in the stock of the company, the respondent indorsed its notes. (R. 9.) In 1921 respondent, as such indorser, was called upon to, and did, pay $68,000, for which he claimed and was allowed a deduction in his income-tax return for that year. (R. 9.)

In 1922 the respondent, being desirous of having some one with financial resources associated with the business of the Bowers Company, sold 1,000 shares of his stock in that company (which had cost him $100,000) to George H. Nolan for $7,500, thus sustaining a loss of $92,500, for which he claimed

and was allowed a deduction in his 1922 return. (R. 9–10.)

During the years 1921 and 1922 respondent also owned, as investments, stock in a number of corporations, and in addition to his activities for and on behalf of the Bowers Company he was a member of and took an active advisory interest in three partnerships engaged in the business of dredging, river and harbor work, and jetty building, mostly in connection with the work of the Bowers Company. (R. 8.)

Respondent's income for 1921 and 1922 was not sufficient to absorb the losses sustained in those years and allowed as deductions by the Commissioner of Internal Revenue, as stated above, with the result that there were unabsorbed balances of $17,768.51 for the year 1921 (R. 9) and $4,985.10 for the year 1922 (R. 10). In his return for 1923 respondent claimed the right to carry these unabsorbed losses forward as "net losses resulting from the operation of any trade or business regularly carried on by the taxpayer," deductible in computing the net income for that year under Section 204 (a) of the Revenue Act of 1921 (*infra*, p. 9). The Commissioner of Internal Revenue disallowed the claim and determined a deficiency accordingly. (R. 11.)

The Board of Tax Appeals held that the evidence did not establish that respondent was engaged in the business of indorsing or guaranteeing notes,

and hence the losses aggregating $68,000 sustained in 1921 by reason of the indorsement and payment of the Bowers Company notes resulted from isolated transactions and therefore "did not result from the operation of a trade or business regularly carried on by the petitioner." (R. 11–12.)

As to the $92,500 loss sustained by respondent upon the sale of Bowers Company stock in 1922, the Board held that the ownership of stock in several corporations as investments, or the sale of some of such stock, did not constitute "a business or trade regularly carried on * * *"; that respondent was neither in the investment business nor the business of dealing in securities, and therefore the loss resulting from the sale of the Bowers Company stock constituted a loss arising from an occasional or isolated transaction "and not from the operation of a business regularly carried on." Accordingly the action of the Commissioner was sustained. (R. 12.)

Upon stipulation (R. 13) the case was taken to the Court of Appeals of the District of Columbia for review (R. 13–17). That court, in reversing the decision of the Board of Tax Appeals (R. 22), held that respondent "was engaged in regularly carrying on the business of dredging, operated by a corporation of which appellant (respondent) was principal owner and active directing head, and to which he devoted all of his time and energies," and that the indorsement and payment of the cor-

porate notes and the selling of the corporate stock was a part of that business (R. 21). This Court granted the Commissioner's petition for a writ of certiorari.

SPECIFICATION OF ERRORS TO BE URGED

The court below erred—

1. In holding that the losses sustained by respondent were "net losses resulting from the operation of any trade or business regularly carried on by the taxpayer" within the meaning of Section 204 (a) of the Revenue Act of 1921.

2. In reversing the decision of the Board of Tax Appeals.

ARGUMENT

The court below held that respondent "was engaged in *regularly carrying on the business of dredging, operated by a corporation* of which appellant (respondent) was principal owner and active directing head, and to which he devoted all of his time and energies" (italics ours), and that the indorsement and payment of the corporate notes and the selling of the corporate stock was a part of that business. (R. 21.)

Thus the court disregarded the corporate entity and held that the business of the Bowers Company was respondent's business. It will be seen that this is the same issue raised in *Hubert Dalton and Florence W. Dalton* v. *Frank C. Bowers, as Executor of the Last Will and Testament of Frank K.*

Bowers, Etc., No. 52, October Term, 1932, now pending in this Court. In its brief in that case the Government argues that even where an individual owns all of the stock of a corporation (as Dalton did), a loss which, if incurred in any business regularly carried on, is incurred in the business of the corporation and not in that of the "taxpayer," can not be used to make up a "net loss." The settled principles which dispose of such a case are discussed at length in that brief. In the instant case Clark owned but a majority of the stock of the corporation. (R. 8.) Others were interested in it and therefore under no circumstances could the corporation be considered as the "alter ego" of Clark. As president and active directing head of the corporation (R. 8) Clark was the agent of the corporation and he indirectly represented the stockholders. His acts were the corporation's acts. The corporation's acts were not his. He was neither in the business of lending money nor selling stock. Accordingly his losses were the result of mere isolated transactions, which under authorities cited in our brief in the *Dalton* case were not attributable to any business regularly carried on by him. The only possible theory which would permit deduction involves a disregard of the corporate entity, and, for reasons stated in the respondent's brief in the *Dalton* case, the entity may not be disregarded.

In view of the close similarity of the two cases it is considered unnecessary to reiterate at length

what has been said in our brief in the *Dalton* case, and therefore we ask that the argument therein be considered as our argument here.

CONCLUSION

The decision of the court below is erroneous and should be reversed.

Respectfully submitted.

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G. A. YOUNGQUIST,
Assistant Attorney General.
WHITNEY NORTH SEYMOUR,
SEWALL KEY,
JOHN H. MCEVERS,
Special Assistants to the Attorney General.

OCTOBER, 1932.

APPENDIX

STATUTES AND REGULATIONS INVOLVED

Revenue Act of 1921, c. 136, 42 Stat. 227, 231:

SEC. 204. (a) That as used in this section the term "net loss" means only net losses resulting from the operation of any trade or business regularly carried on by the taxpayer (including losses sustained from the sale or other disposition of real estate, machinery, and other capital assets, used in the conduct of such trade or business); and when so resulting means the excess of the deductions allowed by section 214 or 234, as the case may be, over the sum of the following: (1) the gross income of the taxpayer for the taxable year, (2) the amount by which the interest received free from taxation under this title exceeds so much of the interest paid or accrued within the taxable year on indebtedness as is not permitted to be deducted by paragraph (2) of subdivision (a) of section 214 or by paragraph (2) of subdivision (a) of section 234, (3) the amount by which the deductible losses not sustained in such trade or business exceed the taxable gains or profits not derived from such trade or business, (4) amounts received as dividends and allowed as a deduction under paragraph (6) of subdivision (a) of section 234, and (5) so much of the depletion deduction allowed with respect to any mine, oil or gas well as is based upon discovery value in lieu of cost.

(b) If for any taxable year beginning after December 31, 1920, it appears upon the production of evidence satisfactory to the

Commissioner that any taxpayer has sustained a net loss, the amount thereof shall be deducted from the net income of the taxpayer for the succeeding taxable year; and if such net loss is in excess of the net income for such succeeding taxable year, the amount of such excess shall be allowed as a deduction in computing the net income for the next succeeding taxable year; the deduction in all cases to be made under regulations prescribed by the Commissioner with the approval of the Secretary.

* * * * *

Treasury Department Regulations 62:

ART. 1601. *Net losses, definition and computation.*—The term "net loss" as used in the statute means only a net loss resulting from the operation during the taxable year of any trade or business regularly carried on by the taxpayer. Included therein are losses from the sale or other disposition of real estate, machinery, and other capital assets used in the conduct of such trade or business. In order to be entitled to claim an allowance for a "net loss" the taxpayer must have suffered an actual net loss in a trade or business during the taxable year. The amount properly allowable may be neither the loss reflected upon the return filed for the purpose of the income tax nor the net loss shown by the taxpayer's profit and loss account, but is to be computed according to the statute, as follows:

(1) In the case of an individual, it is the amount by which the deductions allowed under section 214, excluding:

(a) the amount by which the deductible losses not sustained in such trade or busi-

ness exceed the taxable gain or profits not derived from such trade or business;

* * * * *

(c) the amount of deductions allowed under section 214 not connected with the trade or business,

exceeds the sum of the following:

(a) the gross income of the taxpayer for the taxable year as computed under section 213; and

(b) the amount by which the interest received free from taxation under the provisions of the Act exceeds so much of the interest paid or accrued within the taxable year on indebtedness as is not allowed as a deduction under section 214 (a) (2).

* * * * *

In computing statutory "net loss" the following restrictions are to be noted:

(1) Interest received by the taxpayer on obligations or securities, the interest from which is exempted from taxation must be included in income, but this amount may first be reduced by the amount of any interest paid by the taxpayer on money used to purchase or carry such obligations or securities.

* * * * *

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1932.

No. 180.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE,
Petitioner-Appellant.

vs.

R. P. CLARK, *Respondent-Appellee.*

On Writ of Certiorari to the Court of Appeals of the District of Columbia.

BRIEF FOR RESPONDENT.

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501 Union Trust Bldg.,
Washington, D. C.,
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1932.

No. 180.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE,
Petitioner-Appellant.

vs.

R. P. CLARK, *Respondent-Appellee.*

BRIEF FOR RESPONDENT.

Opinions Below.

The opinion of the Court of Appeals of the District of Columbia (R. 27) is reported in 59 Fed. (2d) 1031. The opinion of the Board of Tax Appeals (R. 15-17) is reported in 19 B. T. A. 859.

Jurisdiction.

The judgment of the Court of Appeals was entered April 11, 1932. Petition for Writ of Certiorari was filed on June 27, 1932, and granted on October 10, 1932. Jurisdiction is conferred upon this Court by Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925.

Statutes Involved.

Revenue Act of 1921, c. 136, 42 Stat. 227, 231.

> Sec. 204. (a) That as used in this section the term "net loss" means only net losses resulting from the operation of any trade or business regularly carried on by the taxpayer (including losses sustained from the sale or other disposition of real estate, machinery and other capital assets, used in the conduct of such trade or business); * * *
>
> (b) If for any taxable year beginning after December 31, 1920, it appears upon the production of evidence satisfactory to the Commissioner that any taxpayer has sustained a net loss, the amount thereof shall be deducted from the net income of the taxpayer for the succeeding taxable year; and if such net loss is in excess of the net income for such succeeding taxable year, the amount of such excess shall be allowed as a deduction in computing the net income for the next succeeding taxable year; the deduction in all cases to be made under regulations prescribed by the Commissioner with the approval of the Secretary.

Question Presented.

Were the net losses sustained in 1921 and 1922 by Respondent Clark, which he seeks to forward and deduct in 1923, net losses "resulting from the operation of any trade or business regularly carried on" by him, within the meaning of Section 204 of the Revenue Act of 1921?

Statement of the Case.

1. The controversy relates to the income and profits tax liability of the respondent, R. P. Clark, for the calendar year 1923. For the calendar year 1921, he sustained a net loss of $17,768.51. For the calendar year 1922 he sustained a net loss of $4,985.18. The respondent sought to deduct the two net losess from his income for 1923 but was denied that privilege by the Commissioner of Internal Revenue

on the ground that they were not net losses resulting from a trade or business regularly carried on by him. On appeal the Board of Tax Appeals sustained the Commissioner, but the Court of Appeals of the District of Columbia reversed the Board, and this Court is now asked to review and reverse or affirm the Court of Appeal's decision.

2. Respondent is a resident of Miami, Florida, and since 1888 has been engaged in river and harbor improvement work, dredging, and jetty building operations. From 1899 he was associated with the Bowers Southern Dredging Company. He was its majority stockholder, its active directing head, and devoted all of his time to its operations (R. 11, 28). In addition to his association with the Bowers Company, Clark in 1921 and 1922 was a member of the partnerships of D. M. Picton & Company, Port Arthur, Texas; The Florida Dredging Company, Miami, Florida, and Megathlin & Clark, Miami, Florida. Megathlin & Clark and The Florida Dredging Company were engaged in the dredging business and D. M. Picton & Company in river and harbor work and jetty building. Respondent Clark took an active advisory interest in these partnerships whose work was mostly in connection with the work of the Bowers Southern Dredging Company (R. 11, 12, 28).

3. At the beginning of the War in 1917 the Bowers Company had many contracts to complete and began to experience financial difficulties. This finally resulted in its business being placed in the hands of a creditors' committee under which it was operated in 1921 (R. 12, 28). Clark became president of the Bowers Company in 1905 and continued in that capacity as long as it continued to operate. During 1921 and until the business was taken over in 1922 by the Clark Dredging Company, he served as managing operator of the company for the creditors. In 1922 the Clark Dredging Company was formed to take over the business and respondent was president of that corporation after its formation (R. 11, 12, 28).

4. The financial difficulties which beset the Bowers Company after the War started in 1917 resulted in its being unable to borrow money from banks without the individual endorsement of respondent, and in order to protect his investment in the company he, at various times, became endorser on the notes of the company. In 1921, as a result of such endorsements, respondent was forced to pay the sum of $68,000 for the company. This amount he took as a deduction for losses in his 1921 income tax return, and it was allowed by the Commissioner (R. 13, 28). In the same return respondent also reported a loss of $9500 incurred in the sale of stock of the Bowers Company, which was allowed (R. 13, 28).

5. In 1922, respondent being desirous of having some one with financial strength associated with the business of the Bowers Company, sold 1000 shares of the stock owned by him in the company, which he had purchased at a cost of $100,000, to George H. Nolan for $7,500. In his tax return for 1922 respondent took a deduction for the loss sustained of $92,500, which the Commissioner allowed (R. 24, 28).

6. The losses hereinabove mentioned being in each year in excess of the income, left the net losses, as above stated, which respondent has sought to deduct from his income of 1923 as net "business losses", coming within the provisions of section 204 of the Revenue Act of 1921.

Summary of Argument.

The "net losses" allowed by the act to be carried forward and deducted are those resulting from the operation of "any trade or business regularly carried on by the taxpayer."

The word "operation" is defined as "the course of action or series of acts by which some result is accomplished." *United States v. Somers,* 164 Fed. 259.

Business is that which occupies the time, attention, and labor of men for the purpose of a livelihood or profit.

The time, attention, and labor of the respondent Clark was devoted to the "business" of dredging, operated by a corporation of which he was principal owner and active directing head, and through partnerships, for the purpose of profit from his investment and in the form of salary. The business had been regularly and continuously carried on by him for a great many years.

Argument.

The respondent's net losses of 1921 and 1922 were net losses resulting from the operation of a "business regularly carried on" by him.

The accepted definition of business is that given in *Flint v. Stone-Tracy Co.*, 220 U. S. 107, 170, decided March 13, 1911, and is as follows:

> "Business" is a very comprehensive term and embraces everything about which a person can be employed. Black's Law Dict. 158, citing Peoples ex rel. Hoyt v. Tax Comrs., 23 N. Y. 242, 244. "That which occupies the time, attention, and labor of men for the purpose of a livelihood or profit." 1 Bouvier's Law Dict. p. 273.

Business is "that which busies or occupies the time, attention, or labor of one as his principal concern, whether for a longer or shorter time; employment, occupation; any particular occupation or employment; mercantile transactions in general; concern; right or occasion of making one's self busy; affairs; transactions." *Territory v. Harris*, 19 Pac. 286.

As stated in the case of *In re Mackey*, 110 Fed. 355, 358:

> The chief occupation or business of one, so far as worldly pursuits are concerned, is that which is of principal concern to him, of some permanency in its nature and on which he chiefly relies for his livelihood or as the means of acquiring wealth, great or small.

And as stated by the Board of Tax Appeals in *Baker v. Commissioner,* 17 B. T. A. 733, 737:

> In order to constitute a "net loss" within the meaning of the statute, it is not necessary that the taxpayer should sustain the loss in his principal business or vocation. The word "business" is qualified by the word "any". The taxpayer is entitled to this benefit where the loss is incurred in "any trade or business regularly carried on" by him. *Oscar K. Eysenbach,* 10 B. T. A. 716. And the term "business" is comprehensive. "Business" is anything "which occupies the time, attention, and labor of men for the purpose of a livelihood or profit." Citing authorities.

What then was the trade or business regularly carried on by the respondent? Since 1888, continuously through the years 1921 and 1922 here involved, he has been engaged in the business of dredging and supervising dredging operations off the coast of Florida and elsewhere. He was actively engaged in this particular business during all of these years, both individually and as the president, majority stockholder and active directing head of the Bowers Southern Dredging Company.

Respondent became associated with the Bowers Southern Dredging Company, as the record shows, in 1899 when it was organized, and continued so until 1922 when he organized the Clark Dredging Company to take over the business. He was president of the Bowers Company from 1905, managed its affairs, and looked after his investment therein, he being for a number of years the majority owner of the stock. When the business was taken in hand by a Creditors' Committee in 1921, he continued as managing operator, and was president of the new Clark Dredging Company which he formed in 1922 to succeed the Bowers Company. In addition to his interest in the Bowers Company, he was also a partner and took an active advisory interest in three other concerns engaged in similar work.

In an early decision of the Board in *Lloyd v. Commis-*

sioner, 8 B. T. A. 1029, it was held that an amount expended by the petitioner in an unsuccessful effort to secure a secret formula for the corporation of which he was president, under an agreement whereby he was to be reimbursed if the venture was successful, was deductible as a loss, and the Board made this further interesting conclusion (P. 1030):

> We are further of the opinion that the loss was "incurred in trade or business" in that the furtherance of the business of the company of which he was president was legally and logically his business.

The furtherance of the business of the company of which respondent was not only president but majority stockholder may likewise be considered as legally and logically his business, for as the Court of Appeals said (R. 29):

> Appellant accordingly was necessarily concerned with the financial conditions and difficulties which beset the business, and he was compelled by circumstances to indorse the company's notes in order to supply it with necessary operating funds. This action was not isolated or occasional but became part of the operation of the business, and helped to carry it on. It is true that appellant did not regularly carry on a business of indorsing notes for profit, but his indorsement of the company's notes was part of the business regularly carried on for the company. It is also true that appellant was not regularly engaged in the business of selling corporate stocks, but the transactions of that character appearing in the record can not be separated from the regular course of business of which they were part, and must not be considered as if wholly independent transactions.

In *Washburn v. Commissioner,* (C. C. A. 8) 51 Fed. (2d) 949, it appears that a lawyer who had organized a number of corporations and enterprises retired from law practice in order to give his entire time to these various enterprises in which he was heavily interested, four of which were tim-

ber holding corporations. In order to open up the timber lands of one of the companies he organized a railroad company, which built a railroad to the property. He was the principal stockholder therein, managed its affairs, and selected its officers and directors. He advanced the money with which to build the railroad and took back stock. In 1922 he sold the stock and sustained a loss which he sought to carry over and deduct in 1923. The Court summed up the situation of the petitioner as follows:

> Petitioner does not claim that he was engaged in the railroad business or that he was a dealer in securities. His position is that his occupation was the personal attention given to the management of the various enterprises in which he had investments for the purpose of making those enterprises successful and profitable; that to this he gave his entire time, and was doing a great deal more than merely guarding his investments; that the loss on the sale of the railroad was occasioned in carrying on his general avocation. (P. 952)

The Court, in reaching its conclusion that the petitioner's loss was one incurred in a trade or business regularly carried on, made this significant statement (P. 953):

> Much is said in argument as to petitioner being engaged solely in holding the securities of the enterprises in which he was interested, and that he was a mere investor receiving the ordinary returns of ownership. A party may have investments in corporate stock, have no particular occupation, and live on the return of his investments. That would not constitute business under the statute in question. *He may, however, take such an active part in the management of the enterprise in which he has investments as to amount to the carrying on of a business.* (Italics ours.)

The view taken by the Circuit Court of Appeals in the *Washburn* case, in the language quoted, and that of the Court of Appeals in the instant case, is in accord with the

decisions of this and other Courts in cases involving the question as to whether corporations are liable to the capital stock tax imposed on the privilege of carrying on or doing business. In those cases it has uniformly been held that where a parent corporation owning the stock of subsidiary corporations and receiving dividends thereon, takes an active part in the management and direction of the subsidiaries, it is carrying on or doing business. *Edwards v. Chile Copper Co.*, 270 U. S. 452; *Phillips v. International Salt Co.*, 274 U. S. 718; *Chevrolet Motor Co. v. United States*, 64 Ct. Cls. 211, certiorari denied, 277 U. S. 585; *Ward Baking Co. v. United States*, 66 Ct. Cls. 456, certiorari denied, 50 Supreme Court, 18.

In the *Edwards v. Chile Copper Co.* case the Court said, at page 455:

> The exemption "when not engaged in business" ordinarily would seem pretty nearly equivalent to when not pursuing the ends for which the corporation was organized, in the cases where the end is profit. In our opinion the plaintiff was liable to the tax. * * * The activities and situation must be judged as a whole. Looking at them as a whole we see that the plaintiff was a good deal more than a mere conduit for the Chile Exploration Company. *It was its brain or at least the efferent nerve without which that company could not move. The plaintiff owned and by indirection governed it, and was its continuing support, by advances from time to time in the plaintiff's discretion.* (Italics ours.)

The Bowers Southern Dredging Company was one of the instrumentalities through which the respondent Clark carried on the dredging business. He was its principal stockholder, president and manager, and devoted all of his time, attention, and energy to its affairs, for the purpose of profit. He was, to paraphrase the language of the court in the *Chile Copper Co.* case, its brains, the efferent nerve by which it moved, and the indorsement by him of its notes, which resulted in his loss, as well as the sacrifice of his

stock, were steps taken to energize the corporation, sustain its life or existence, and continue the business which was his principal concern as a means of acquiring wealth or profit.

The decision of the Board of Tax Appeals in the case of this respondent was adverse, the Board stating, with respect to his loss of $68,000 resulting from indorsement of notes for the Bowers Southern Dredging Company, that so far as the record showed these were the only notes ever endorsed by him for the company and there was nothing to indicate that acting as endorser or guarantor constituted a business or trade with him.

The Court of Appeals in reversing the decision of the Board points to several more recent decisions in similar cases where the conclusions reached by the Board are inconsistent with its conclusion in this case. They are *Anthony v. Commissioner*, 20 B. T. A. 5; *Averill v. Commissioner*, 20 B. T. A. 1196, 1199, and *Heller v. Commissioner*, 25 B. T. A. 259.

An analysis of the decisions in question will show that the situation involved in each instance is very similar to that in respondent's case. In the *Anthony* case, the business was the retailing of ready to wear furnishings for men, women and children. It was first a partnership and then corporations were organized. In the *Averill* case, the taxpayer was interested in many enterprises in various activities, all in corporate form. In the *Heller* case, the petitioners were stockholders in and managed and operated the business of several corporations engaged in retailing ladies' ready to wear clothing. In the respondent's case the business was that of river and harbor improvement, dredging and jetty building, operated through three concerns, in which he was a partner, and a corporation in which he was the principal shareholder, president and manager.

With equal force, it can be said, as in these three cases, if

that be the determining factor, that respondent used both capital and knowledge in the business of managing concerns engaged in the dredging, river and harbor improvement, and jetty building business.

The situation is probably even more pronounced in the instant case than in *Potter v. Commissioner*, 18 B. T. A. 549, decided in 1929 by the Board. Potter had been for a number of years interested in various hotel enterprises. He owned and operated the Clarendon Hotel at Sea Breeze, Fla., until it burned down. A corporation was formed for the purpose of building and operating a hotel of the same name on the same site. Potter acquired $100,000 of the $250,000 issued preferred stock and $275,000 of the $300,000 issue common stock of the corporation. He actively operated the hotel as managing-director for a salary of $3,000 per year. The corporation obtained a loan of $150,000 and as a consideration for making the loan the lender acquired 50 per cent of the outstanding common stock belonging to Potter. Subsequently the parties became involved in litigation, the outcome of which was the sale by Potter to his opponents of his stockholdings at a considerable loss, which loss the Board held to have been incurred in a trade or business regularly carried on by Potter. In both instances the taxpayer was interested as a stockholder and manager-director in an activity from which he earned his livelihood—Mr. Potter, in the hotel business, and Mr. Clark in the dredging business. Each sustained losses in the sale of stock in one of the enterprises with which he was connected and in assisting his corporation to obtain loans or working funds. They were not mere investors but made the business in which their funds were invested the subject of their personal and individual attention, receiving salary in addition to the return from the investment. Quoting from the opinion in the *Potter* case (page 553):

> The picture presented shows clearly that the investment and the personal management were closely re-

> lated, each dependent on the other, the two combined producing the income received by this taxpayer, and that the knowledge, experience, work and investment were all in respect to one definite and distinct line of business, * * *.

The fact that the respondent in endorsing the notes of the Bowers Southern Dredging Company and paying same and the selling of some of his shares of the stock to improve the financial standing of the company was, in addition to assisting and aiding his business in the several partnerships, safeguarding his investments by providing funds and financial assistance needed by the corporation, does not—to adopt the language of the Board of Tax Appeals in *Comrades v. Commissioner,* 21 B. T. A. 213, 215—stamp these activities as merely an incident of his service as an officer of the corporation or as merely incident to his ownership of the stock.

For other Board decisions dealing with the subject of losses incurred in trade or business regularly carried on, see:

Heaslet v. Commissioner, 23 B. T. A. 50;
Lovering v. Commissioner, 21 B. T. A. 1260.

CONCLUSION.

The facts in this case show clearly that the net losses sustained by respondent in 1921 and 1922 were losses resulting from the operation of a trade or business regularly carried on by him within the intent and meaning of Section 204 of the Revenue Act of 1921, as construed by the Court of Appeals.

The judgment of the Court of Appeals should, therefore, be affirmed.

Respectfully submitted,

WM. S. HAMMERS,
Counsel for Respondent.

SUPREME COURT OF THE UNITED STATES.

No. 180.—October Term, 1932.

David Burnet, Commissioner of Internal Revenue, Petitioner, *vs.* R. P. Clark. } On Writ of Certiorari to the Court of Appeals of the District of Columbia.

[December 12, 1932.]

Mr. Justice McReynolds delivered the opinion of the Court.

Respondent Clark's income tax return for 1921 showed net loss exceeding $17,000; for 1922 net loss of about $5,000. He claimed these should be deducted from gains reported for 1923, under Section 204 (a) and (b),* Revenue Act of 1921, c. 136, 42 Stat.

*Revenue Act, 1921: "Sec. 204 (a). That as used in this section the term 'net loss' means only net losses resulting from the operation of any trade or business regularly carried on by the taxpayer (including losses sustained from the sale or other disposition of real estate, machinery, and other capital assets, used in the conduct of such trade or business); and when so resulting means the excess of the deductions allowed by section 124 or 234, as the case may be, over the sum of the following: (1) The gross income of the taxpayer for the taxable year, (2) the amount by which the interest received free from taxation under this title exceeds so much of the interest paid or accrued within the taxable year on indebtedness as is not permitted to be deducted by paragraph (2) of subdivision (a) of section 214 or by paragraph (2) of subdivision (a) of section 234, (3) the amount by which the deductible losses not sustained in such trade or business exceed the taxable gains or profits not derived from such trade or business, (4) amounts received as dividends and allowed as a deduction under paragraph (6) of subdivision (a) of section 234, and (5) so much of the depletion deduction allowed with respect to any mine, oil or gas well as is based upon discovery value in lieu of cost.

"(b) If for any taxable year beginning after December 31, 1920, it appears upon the production of evidence satisfactory to the Commissioner that any taxpayer has sustained a net loss, the amount thereof shall be deducted from the net income of the taxpayer for the succeeding taxable year; and if such net loss is in excess of the net income for such succeeding taxable year, the amount of such excess shall be allowed as a deduction in computing the net income for the next succeeding taxable year; the deduction in all cases to be made under regulations prescribed by the Commissioner with the approval of the Secretary."

227, 231. The Commissioner of Internal Revenue ruled otherwise and the Board of Tax Appeals approved. The Court of Appeals, District of Columbia, reversed the Board's action. The matter is here upon certiorari.

From 1899 until 1922 respondent was closely connected with the Bowers Southern Dredging Company which did river and harbor improvement work, dredging and jetty building. He was majority stockholder, active head, after 1905 president, and devoted himself largely to its affairs. During 1921 and 1922 he was a member of three partnerships similarly engaged and often associated with the Bowers Company. Also, he owned and held as investments shares of a number of corporations. He was not in the investment business.

After 1917 the Bowers Company encountered continuous financial difficulties. To protect his interest therein, at sundry undisclosed times respondent endorsed the company's obligations to the banks. In 1921 a creditors' committee took charge and thereafter respondent conducted the corporate affairs as managing director. A new concern took over the entire assets and business in 1922.

Because of his endorsements respondent paid $68,000 for the Company during 1921. He claimed and was allowed to deduct the sum thus lost upon his return for that year. During the same year he also lost $9,500 through sale of the corporation's stock and in 1922 he sustained a similar loss amounting to $92,500. For both these sums appropriate deductions were permitted.

After considering all the circumstances, the Collector held respondent's losses did not result "from the operation of any trade or business regularly carried on by the taxpayer," and could not be deducted from gains of succeeding years. The Board of Tax Appeals approved. Among other things, it said—

> "In order for the losses here involved to be deductible in determining taxable income for 1923, they must be net losses resulting from the operation of a trade or business regularly carried on by the petitioner and not from isolated and occasional transactions.
>
> "With respect to the loss of $68,000 resulting from the petitioner's endorsement of the Bowers Company notes, he testified that in endorsing the notes he was seeking to protect his

investment in its stock. Aside from endorsing an undisclosed number of notes of this company there is nothing in the record to indicate that acting as endorser or guarantor constituted a business or trade with the petitioner. So far as the record shows these were the only notes ever endorsed by the petitioner for the Bowers Company or for any other company or person. From the facts in the case we are of the opinion that the loss did not result from the operation of a trade or business regularly carried on by the petitioner but resulted from isolated or occasional transactions. . . .

"With respect to the remaining losses resulting from the sale of the Bowers Company stock in 1921 and 1922, we do not think the petitioner's ownership of stock in a number of corporations which he held as an investment during 1921 and 1922 or the sale of some of such stock in those years constituted a business or trade regularly carried on by him. As to his being in the investment business, the petitioner testified as follows: 'Q. Would you say you were in the investment business, Mr. Clark?' 'A. No. sir.'

"Since the petitioner was not in the investment business or engaged in the business of a dealer in securities, we think the losses resulting from the sale of the Bowers Company stock in 1921 and 1922 constituted losses arising from occasional or isolated transactions and not from the operation of a business regularly carried on . . . ."

In support of the contrary view the District Court of Appeals said—

"It appears that during the times in question appellant was engaged in regularly carrying on the business of dredging, operated by a corporation of which appellant was principal owner and active directing head, and to which he devoted all of his time and energies. Appellant accordingly was necessarily concerned with the financial conditions and difficulties which beset the business, and he was compelled by circumstances to indorse the company's notes in order to supply it with necessary operating funds. This action was not isolated or occasional but became part of the operation of the business, and helped to carry it on. It is true that appellant did not

regularly carry on a business of indorsing notes for profit, but his indorsement of the company's notes was part of the business regularly carried on for the company. It is also true that appellant was not regularly engaged in the business of selling corporate stocks, but the transactions of that character appearing in the record can not be separated from the regular course of business of which they were part, and must not be considered as if wholly independent transactions."

We agree with the Commissioner and the Board of Tax Appeals. The judgment below must be reversed.

The respondent was employed as an officer of the corporation; the business which he conducted for it was not his own. There were other stockholders. And in no sense can the corporation be regarded as his *alter ego,* or agent. He treated it as a separate entity for taxation; made his own personal return and claimed losses through dealings with it. He was not regularly engaged in endorsing notes, or buying and selling corporate securities. The unfortunate endorsements were no part of his ordinary business, but occasional transactions intended to preserve the value of his investment in capital shares.

A corporation and its stockholders are generally to be treated as separate entities. Only under exceptional circumstances—not present here—can the difference be disregarded.

Reversed.

A true copy.

Test:

Clerk, Supreme Court, U. S.